

MALTA

OUTLINE

LIST OF ABBREVIATIONS.....	IV
LIST OF LEGAL REFERENCES.....	V

PART I. IMPLEMENTATION OF THE DIRECTIVE VI

1. INTRODUCTION.....	VI
1.1. GENERAL INFORMATION ON THE IMPLEMENTATION OF THE DIRECTIVE	VI
1.2. TAX TREATMENT OF INTEREST AND ROYALTY PAYMENTS UNDER GENERAL TAX LAW	VI
1.2.1. Domestic rules	vi
1.2.2. Treaties	vii
2. SCOPE.....	VIII
2.1. PAYMENTS	VIII
2.1.1. Concept of interest.....	viii
2.1.2. Concept of royalties	viii
2.2. COMPANIES.....	VIII
2.2.1. Types of companies benefiting from implementing provisions (Art. 3(a)(i))	viii
2.2.2. Residence requirement (Art. 3(a)(ii)).....	ix
2.2.3. Subject-to-tax requirement (Art. 3(a)(iii)).....	ix
2.2.4. Associated company (Art. 3(b)).....	ix
2.2.5. Beneficial ownership (Art. 1(4))	ix
2.3. PERMANENT ESTABLISHMENTS	X
2.3.1. Definition (Art. 3(c)).....	X
2.3.2. Application of source rules (Art. 1(2)).....	X
2.3.3. 'Tax-deductible expense' requirement (Art. 1(3)).....	X
2.3.4. Beneficial ownership (Art. 1(5))	X
2.3.5. Permanent establishment in a third country (Art. 1(8))	X
3. PROCEDURE	XI
3.1. MINIMUM HOLDING PERIOD (ART. 1(10))	XI
3.1.1. General	xi
3.1.2. Relief before the holding period requirement is satisfied	xi
3.1.3. Appeals	xi
3.2. ATTESTATION (ART. 1(11) AND 1(13))	XI
3.2.1. General	xi
3.2.2. Appeals	xi
3.2.3. Relief before the holding period requirement is satisfied	xi
3.3. DECISION ON APPLICATION OF THE RELIEF (ART. 1(12))	XI
3.3.1. General	xi
3.3.2. Supporting documents.....	xi
3.3.3. Appeals	xii
3.4. APPLICATION FOR REFUND (ART. 1(15) AND 1(16)).....	XII
3.4.1. General	xii
3.4.2. Appeals	xii
4. FRAUD AND ABUSE (ART. 5).....	XIII
4.1. MEASURES UNDER ART. 5(1) OF THE DIRECTIVE.....	XIII
4.1.1. Domestic	xiii
4.1.2. Agreement-based	xiii

4.2.	MEASURES UNDER ART. 5(2) OF THE DIRECTIVE.....	XIII
4.3.	COMPARISON WITH SIMILAR MEASURES UNDER PARENT-SUBSIDIARY AND MERGER DIRECTIVES	XIII
5.	SUMMARY	XIV
PART II. THE AGREEMENT		XV
	INTRODUCTION.....	XV
1.	SCOPE.....	XV
1.1.	PAYMENTS	XV
1.1.1.	Concept of interest.....	xv
1.1.2.	Concept of royalties	xv
1.2.	COMPANIES.....	XV
1.2.1.	Types of companies benefiting from Art. 15(2) of the Agreement	xv
1.2.2.	'Affiliated' companies	xv
1.2.3.	Residence requirement.....	xv
1.2.4.	Subject-to-tax requirement	xv
2.	PROCEDURE	XVI
3.	SUMMARY	XVI
	ANNEX.....	XVII

LIST OF ABBREVIATIONS

Agreement	Agreement between the European Community and the Swiss Confederation providing for measures equivalent to those laid down in Council Directive 2003/48/EC on taxation of savings income in the form of interest payments
Directive	Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payment made between associated companies of different Member States
ITA	Income Tax Act, Chapter 123 of the Laws of Malta
ITMA	Income Tax Management Act, Chapter 372 of the Laws of Malta
Merger Directive	Council Directive 90/434/EEC of 23 July 1990 on the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States
OECD	Organization for Economic Cooperation and Development
OECD MC	OECD Model Tax Convention 2003
Parent-Subsidiary Directive	Council Directive 90/435/EEC of 23 July 1990 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States



LIST OF LEGAL REFERENCES

- Legal Notice 267 of 2004.
- Income Tax Act, Chapter 123 of the Laws of Malta.
- Income Tax Management Act, Chapter 372 of the Laws of Malta.

PART I. IMPLEMENTATION OF THE DIRECTIVE

1. INTRODUCTION

1.1. GENERAL INFORMATION ON THE IMPLEMENTATION OF THE DIRECTIVE

The Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payment made between associated companies of different Member States (the "Directive") was implemented into local legislation by means of Art. 4 of Legal Notice 267 of 2004, entitled the 'European Union Directives Regulation, 2004', which provides that:

"The Directive of 3 June, 2003 adopted by the Council of the European Communities on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States (2003/49/EC) (hereinafter in this regulation referred to as the "Interest and Royalties Directive") shall have effect in relation to the Income Tax Acts."

The table below shows the relevant provisions of national laws implementing the Directive:

<u>Articles of the Directive</u>	<u>Relevant sections of national laws</u>
Art. .1	Art. 4. Legal Notice 267 of 2004 / Art. 12 ITA
Art. .2	Art. 4. Legal Notice 267 of 2004 / Art. 12 ITA
Art. .3	Art. 4. Legal Notice 267 of 2004 / Art. 12 ITA
Art. .4	Art. 4. Legal Notice 267 of 2004 / Art. 12 ITA
Art. .5	Art. 4. Legal Notice 267 of 2004 / Art. 12 ITA
Art. .7	Art. 4. Legal Notice 267 of 2004 / Art. 12 ITA

1.2. TAX TREATMENT OF INTEREST AND ROYALTY PAYMENTS UNDER GENERAL TAX LAW

1.2.1. Domestic rules

Interest and royalties arising outside Malta and received by a person resident in Malta are chargeable to tax in Malta in the hands of the recipient at the rate of 35% in the case of companies and at the rate applicable under the progressive system of taxation in the case of individuals.

Article 12(1)(c) of the ITA exempts from tax in Malta interest and royalties arising to persons who are not resident in Malta unless such persons are engaged in a trade or business in Malta through a permanent establishment situated in Malta and the royalties or interest are effectively connected with the permanent establishment and provided that the recipient of the interest or royalty is the beneficial owner thereof and is not owned and controlled by, directly or indirectly, nor acts on behalf of a person who is ordinarily resident and domiciled in Malta.

Where the exemption stipulated in Art. 12(1)(c) ITA does not apply, the said interest or royalties are chargeable to tax in Malta and the payer is required to withhold tax, in terms of Art. 73 ITA, on any such payment at the following rates:

- i) 35% where the recipient is a company not resident in Malta,
and
- ii) 25% in all other cases.

Interest and royalty expenses wholly and exclusively incurred in the production of chargeable income are under Art. 14 ITA deductible expenses for the purposes of determining taxable income.

Malta has no thin capitalisation or other similar rules.

1.2.2. Treaties

Malta has concluded tax treaties with all EU Member States, except Greece, Ireland and Spain (see Annex). Malta's double taxation treaties are all negotiated on the basis of the OECD MC and as a result all contain provisions essentially equivalent to Arts. 11 and 12 of the OECD MC. In contrast to the OECD MC Malta's tax treaties, however, usually allow taxation of royalties in the state of source.

It is not however uncommon for Malta's treaties to permit the source country to withhold tax on outbound royalty payments typically at a rate between 5% and 15%. In view of the fact that in terms of local law royalties arising to a person not resident in Malta are, unless effectively connected to a local permanent establishment, exempt from tax in Malta this variation is of no consequence in the case of royalties arising in Malta to a non-resident taxpayer.

2. SCOPE

2.1. PAYMENTS

2.1.1. Concept of interest

a. Definition

Due to the manner in which the Directive has been implemented the definition of the term 'Interest' for the purposes of payments falling within the scope of the Directive is identical to the definition found in the Directive.

b. Exclusion of hybrid financial arrangements (Art. 4(1) b)-d))

Malta has not used its option to exclude payments under financial arrangements listed in Art. 4(1) b) c) d) of the Directive.

c. Exclusion of interest reclassified as profit distribution or conflicting arm's length (Art. 4(1) a) and Art. 4(2))

Malta has not used its option to deny the exemption to interest reclassified as profit distributions and no other rules limiting exemptions under the Directive in situations of special relationship in terms of Art. 4(2) have been applied.

2.1.2. Concept of royalties

a. Definition

Due to the manner in which the Directive has been implemented the definition of the term 'royalty' for the purposes of payments falling within the scope of the Directive is identical to the definition found in the Directive.

b. Classification of revenue from leasing and software

Due to the manner in which the Directive has been implemented the scope is identical to that provided for in the Directive.

c. Exclusion of royalties reclassified as profit distribution or conflicting arm's length (Art. 4(1) a) and Art. 4(2))

Same as 2.1.1. *c. Exclusion of interest reclassified as profit distribution or conflicting arm's length (Art. 4(1) a) and Art. 4(2))* above.

2.2. COMPANIES

2.2.1. Types of companies benefiting from implementing provisions (Art. 3(a)(i))

a. Other types of entities

Due to the manner in which the Directive has been implemented the scope is strictly speaking restricted to the entities listed in the Directive.

However please note that the exemption from local tax provided for under Art. 12(1)(c) of the ITA (See 1.2.1. Domestic rules above) equally applies to all persons whether natural or legal, corporate or otherwise.

b. Hybrid entities

The treatment outlined in point 1. INTRODUCTION above is unaffected by the legal nature / status of the recipient of the interest of royalty payment.

Issues may arise from a definitional perspective on the classification of payments made by 'Hybrid entities' but there is little guidance/certainty in this regard and the issues must be assessed on a case-by-case basis.

2.2.2. Residence requirement (Art. 3(a)(ii))

a. Implementation of the requirement

Due to the manner in which the Directive has been implemented this requirement has strictly speaking been implemented in the manner expressly provided for in the Directive.

However please note that the exemption from local tax provided for under Art. 12(1)(c) of the ITA (see 1.2.1. Domestic rules above) equally applies to all persons whether natural or legal, corporate or otherwise, irrespective of their country of residence.

b. Application of the requirement in dual residence cases

Due to the manner in which the Directive has been implemented this requirement has strictly speaking been implemented in the manner expressly provided for in the Directive.

However please note that the exemption from local tax provided for under Art. 12(1)(c) of the ITA (See 1.2.1. Domestic rules above) equally applies to all persons irrespectively.

2.2.3. Subject-to-tax requirement (Art. 3(a)(iii))

No 'subject-to-tax' requirement exists in the Maltese law.

2.2.4. Associated company (Art. 3(b))

Due to the manner in which the Directive has been implemented this requirement has strictly speaking been implemented in the manner expressly provided for in the Directive.

However please note that the exemption from local tax provided for under Art. 12(1)(c) of the ITA (see 1.2.1. Domestic rules, above) equally applies irrespective of whether the parties are related or otherwise.

Malta has not availed itself of the option contemplated in Art. 3(b) of the Directive to use the criterion of a minimum holding of voting rights.

2.2.5. Beneficial ownership (Art. . 1(4))

Due to the manner in which the Directive has been implemented this requirement has strictly speaking been implemented in the manner expressly provided for in the Directive.

No guidance, case-law or administrative practice is available on the interpretation of this requirement.

2.3. PERMANENT ESTABLISHMENTS

2.3.1. Definition (Art. 3(c))

The permanent establishment notion is known to Maltese tax law but is not expressly defined for local tax purposes. The term is in fact only defined within the context of Malta's double taxation treaties.

While there is no definition of the term 'permanent establishment' for domestic tax purposes the term is generally accepted to have the same meaning for domestic tax purposes as is ascribed to it in Art. 5 of the OECD MC.

2.3.2. Application of source rules (Art. 1(2))

While there is no definition of the term 'permanent establishment' for domestic tax purposes the term is generally accepted to have the same meaning for domestic tax purposes as is ascribed to it in Art. 5 of the OECD MC. We are unaware of any instances in practice where a narrower definition has been applied.

2.3.3. 'Tax-deductible expense' requirement (Art. 1(3))

Within the context of the Directive we are not aware of any instances in which Malta has refused to recognise a payment as a tax-deductible expense because it considered the expense as not attributable to the permanent establishment.

2.3.4. Beneficial ownership (Art. 1(5))

Due to the manner in which the Directive has been implemented this requirement has strictly speaking been implemented in the manner expressly provided for in the Directive.

No guidance, case-law or administrative practice is available on the interpretation of the term 'effectively connected' or the 'subject-to tax' requirement.

2.3.5. Permanent establishment in a third country (Art. 1(8))

Due to the manner in which the Directive has been implemented this requirement has strictly speaking been implemented in the manner expressly provided for in the Directive.

However please note that this notwithstanding the exemption from local tax provided for under Art. 12(1)(c) (see 1.2.1. Domestic rules, above) equally applies irrespectively. As a result the local interpretation of the 'business is wholly or partly carried on through that permanent establishment' in a third state requirement is rendered superfluous.

3. PROCEDURE

The exemption applies at source and it is the responsibility of the payor / the withholding agent to be satisfied that the conditions for the application of the exemption subsist.

3.1. MINIMUM HOLDING PERIOD (ART. 1(10))

No holding period required.

3.1.1. General

N/a.

3.1.2. Relief before the holding period requirement is satisfied

N/a.

3.1.3. Appeals

N/a.

3.2. ATTESTATION (ART. 1(11) AND 1(13))

No attestation required.

3.2.1. General

N/a.

3.2.2. Appeals

N/a.

3.2.3. Relief before the holding period requirement is satisfied

N/a.

3.3. DECISION ON APPLICATION OF THE RELIEF (ART. 1(12))

No formal decision is required.

3.3.1. General

N/a.

3.3.2. Supporting documents

N/a.

3.3.3. Appeals

N/a.

3.4. APPLICATION FOR REFUND (ART. 1(15) AND 1(16))

Malta generally applies an exemption at source system.

3.4.1. General

Should tax have been withheld at source the taxpayer is in terms of Art. 73 ITA and Art. 48 ITMA entitled to submit a tax return in which the local tax liability must be declared and any amount withheld in excess of the tax due by the taxpayer in terms of the tax return would be refundable.

A tax refund is typically paid within 8 months from the day on which is it due.

3.4.2. Appeals

A refusal to refund would imply a disagreement by the tax authorities as to the tax due in Malta by the taxpayer for the relevant period. In such a case the usual objection and appeals procedure would apply in terms of which the taxpayer may object to an assessment raised by the Commissioner for Inland Revenue and, in the event that the Commissioner does not withdraw his assessment the tax payer is entitled to file an appeal before the Board of Special Commissioners from whose decision the taxpayer has a limited right of appeal, to the Courts of Appeal, on any point of law.

4. FRAUD AND ABUSE (Art. 5)

The implementing legislation makes no reference to any anti-abuse provisions.

4.1. MEASURES UNDER ART. 5(1) OF THE DIRECTIVE

4.1.1. Domestic

In terms of domestic law the exemption provided for under Art. 12 of the ITA (see 1.2.1. Domestic rules, above) only applies insofar as the recipient of the interest or royalty is not owned and controlled by, directly or indirectly, nor acts on behalf of a person who is ordinarily resident and domiciled in Malta. The compatibility of this anti-abuse rule within the context of interest and royalty payments falling within the purview of the Directive is questionable.

4.1.2. Agreement-based

N/a.

4.2. MEASURES UNDER ART. 5(2) OF THE DIRECTIVE

Although no specific anti-abuse provisions have been enacted in this regard, Art. 51 ITA provides the Commissioners of Inland Revenue with far reaching powers to strike down and disregard, for tax purposes, any artificial, fictitious or abandoned scheme which reduces the amount of tax payable by a taxpayer.

Additionally, should a taxpayer implement any scheme with the sole or main purpose of avoiding, reducing or postponing liability to Maltese tax, or of obtaining any refund or set-off of tax, the Commissioner is entitled to assess the taxpayer to tax so as to effectively nullify or modify the scheme and the consequent advantage (Art. 51(2) ITA).

4.3. COMPARISON WITH SIMILAR MEASURES UNDER PARENT-SUBSIDIARY AND MERGER DIRECTIVES

There is no difference in implementation between the three directives. The local authorities have not issued any formal statement as to the manner in which the various provisions are to be interpreted, as a result it is impossible to determine whether there is in fact any variation in interpretation between the three.



5. SUMMARY

Malta has comprehensively implemented the Directive.

Doubt exists regarding the compatibility of a local anti-abuse provision which would limit the exemption contemplated in Art. 12 ITA to situations in which the recipient of the interest or royalty is not owned and controlled by, directly or indirectly, nor acts on behalf of a person who is ordinarily resident and domiciled in Malta. The compatibility of this anti-abuse rule within the context of interest and royalty payments falling within the purview of the Directive is questionable.

PART II. THE AGREEMENT

INTRODUCTION

To the best of our knowledge Agreement between the European Community and the Swiss Confederation providing for measures equivalent to those laid down in Council Directive 2003/48/EC on taxation of savings income in the form of interest payments (the "Agreement") has not been ratified / incorporated into local law.

In terms of the current status of local tax law no further action is however required for the object and purpose of Art. 15 of the Agreement to be achieved on outbound payments of dividends, interests and royalties.

1. SCOPE

1.1. PAYMENTS

1.1.1. Concept of interest

For local tax purposes the term 'interest' is not expressly defined. It is generally accepted by practitioners that for the purposes of the Agreement the Directive / OECD MC definitions should apply.

1.1.2. Concept of royalties

For local tax purposes the term 'royalty' is not expressly defined. It is generally accepted by practitioners that for the purposes of the Agreement the Directive definition should apply.

1.2. COMPANIES

1.2.1. Types of companies benefiting from Art. 15(2) of the Agreement

The treatment equally applies to all persons irrespective of their (legal) form.

1.2.2. 'Affiliated' companies

The treatment equally applies to all persons irrespective of the relationship between the parties.

1.2.3. Residence requirement

The treatment equally applies to all persons irrespective of their country of residence.

1.2.4. Subject-to-tax requirement

In terms of local law this requirement is not relevant.



2. PROCEDURE

As under the interest and royalties directive the exemption at source procedure applies.

3. SUMMARY

Notwithstanding the fact that the required instrument of ratification does not appear to have been formalised the object and purpose of the Agreement appears to be adequately reflected/addressed in the current provisions of the local tax laws.

ANNEX

Table of the maximum withholding tax rates on interest and royalty payments under the tax treaties between Malta and the EU Member States.

<u>EU Member State</u>	<u>Interest (%)</u>	<u>Royalties (%)</u>
<u>Austria</u>	5	<u>10</u>
<u>Belgium</u>	10	<u>10</u>
<u>Czech Republic</u>	<u>0</u>	5
<u>Cyprus</u>	<u>10</u>	<u>10</u>
<u>Denmark</u>	<u>0</u>	<u>0</u>
<u>Estonia</u>	<u>10</u>	<u>10</u>
<u>Finland</u>	<u>10</u>	10
<u>France</u>	<u>10</u>	<u>10</u>
<u>Germany</u>	<u>0</u>	<u>0</u>
Hungary	10	10
<u>Italy</u>	10	<u>10</u>
<u>Latvia</u>	10	10
<u>Lithuania</u>	<u>10</u>	<u>10</u>
<u>Luxembourg</u>	<u>0</u>	<u>10</u>
<u>Netherlands</u>	<u>10</u>	<u>10</u>
<u>Poland</u>	<u>10</u>	<u>10</u>
<u>Portugal</u>	<u>10</u>	<u>10</u>
<u>Slovak Republic</u>	<u>0</u>	5
<u>Slovenia</u>	5	5
<u>Sweden</u>	<u>0</u>	<u>0</u>
<u>United Kingdom</u>	<u>10</u>	<u>10</u>